



Using Environmental Insurance in DoD Property Transfers: A NEW TOOL FOR MANAGING CLEANUP RISK

This fact sheet provides information on environmental insurance and discusses the main types of environmental insurance available.

An increased understanding of the risks related to environmental cleanup and redevelopment of contaminated properties, such as brownfields and Superfund sites, has prompted development of new environmental insurance products. The coverage options now available allow parties—such as the Local Redevelopment Authority (LRA), developer, lender, and lessee—to tailor insurance policies specifically to their situation in managing the potential legal, financial, and environmental risks that may be associated with redeveloping former DoD property. Additionally, where the LRA assumes responsibility for cleaning up property transferred using the Early Transfer Authority (ETA), the LRA can purchase environmental insurance to insure itself against possible cost overruns during its cleanup of the installation property. Insurance coverage for costs related to the interruption of business resulting from newly discovered contamination can also be obtained.

What is Early Transfer Authority (ETA)?

ETA is a Comprehensive Environmental Response, Compensation and Liability Act (CERCLA) provision §120(h)(3)(C) that allows DoD to transfer property before completing cleanup by allowing DoD to defer the CERCLA covenant that all necessary remedial action has been completed before transfer. While DoD can continue the cleanup under ETA, the LRA may opt to assume responsibility for the cleanup of the property in order to more fully integrate cleanup actions with redevelopment priorities. ETA is not itself privatization, but it can facilitate privatization by allowing DoD to transfer the property and the responsibility for the execution of cleanup activities.

Environmental insurance can cover some of the potential risks associated with the redevelopment of DoD property, such as:

- Cost overruns when the estimated cost of the cleanup plan is exceeded
- Tort liability resulting from injuries that occur to parties involved in the cleanup
- Business or work stoppage caused by discovery of previously unknown contaminants
- Claims against third parties associated with ongoing operations
- Claims against third parties conducting remediation activities
- Failure of the initial remedy before transfer
- New contamination discovered after acquiring the property.

Environmental insurance may make a former DoD property more attractive to a potential buyer or transferee. Insuring the property can help minimize and quantify the risk. This may increase the value of the property and protect against the cost of cleanup outweighing the property's fair market value. Environmental insurance may also aid a redeveloper in obtaining sufficient financing for a redevelopment project. Several insurance policies

Privatizing Cleanup

Unlike outsourcing, where the federal government retains the asset but delegates its management to an outside entity, privatization allows the federal government to divest itself of an asset and the costs associated with maintaining the asset. In the Base Realignment and Closure (BRAC) context, privatization of cleanup means that DoD would transfer both the property and the cleanup responsibility to another entity, although the legal liability for the contamination and the efficacy of the remedial action remains with DoD.



provide for the lender to be named as an additional insured, which can potentially reduce the lender's concerns regarding future liability and assist in stimulating financing and investment.

WHAT ARE THE DIFFERENT TYPES OF ENVIRONMENTAL INSURANCE POLICIES?

Several types of environmental insurance policies are available for parties interested in purchasing, selling, financing, cleaning up, or redeveloping contaminated properties. These policies can help manage the potential legal, financial, and environmental risk. The most common types are *pollution legal liability*, *cleanup cost cap or stop gap insurance*, *property transfer*, and *brownfields restoration and redevelopment insurance*. While these general categories encompass a large portion of the environmental insurance market, insurance providers also offer a number of additional, more specific options (e.g., secured creditor insurance).

POLLUTION LEGAL LIABILITY INSURANCE is designed to cover claims against the current or previous property owner arising from cleanup, bodily injury, or property damage. Both known and unknown pre-existing contamination may be covered in the policy. This type of coverage can be used either before or after the cleanup is conducted. Policies providing coverage for business interruptions resulting from discovery of contamination are common under pollution legal liability coverage.

CLEANUP COST CAP OR STOP GAP INSURANCE covers instances where actual cleanup costs exceed the estimated cost. Insurance providers now offer cleanup cost cap or stop gap coverage, which will pay up to an agreed-upon amount once the cleanup costs exceed a designated amount. The policy can also be structured to include coverage for offsite cleanup costs on surrounding properties. The coverage typically ends after completion of the cleanup and certification that the cleanup has been completed.

CERCLA §120(h)(3)

In the case of the sale or other transfer of any parcel of [federal real property]...the deed entered into for the sale or transfer of such property by the United States to any other person or entity shall contain:

- (ii) a covenant warranting that -
 - (I) all remedial action necessary to protect human health and the environment with respect to any such substance remaining on the property has been taken before the date of such transfer, and
 - (II) any additional remedial action found to be necessary after the date of such transfer shall be conducted by the United States; and
- (iii) a clause granting the United States access to the property in any case in which remedial action or corrective action is necessary after the date of such transfer.

PROPERTY TRANSFER INSURANCE is designed to cover claims arising from pre-existing unknown contamination and known contamination below reportable levels. This type of insurance is similar to the pollution legal liability insurance coverage, but is more focused on the property transfer scenario. The seller, buyer, and lender can all be named insureds on the property transfer insurance policy.

BROWNFIELDS RESTORATION AND REDEVELOPMENT INSURANCE is designed to cover a site with known environmental contamination for which cleanup and development activities are planned. It is a combination of property transfer insurance and cleanup cap type insurance, and can include the business interruption coverage discussed under pollution legal liability.

USE OF ENVIRONMENTAL INSURANCE IN DoD PROPERTY TRANSFERS

As part of every transfer of DoD property, the transferee is afforded protection from liability for environmental contamination through the Comprehensive Environmental Response, Compensation and Liability Act (CERCLA) §120(h) covenant. Under CERCLA §120(h)(3), the



federal government is responsible for cleaning up any contamination that can be attributed to DoD activities discovered after the property is transferred. For Base Realignment and Closure (BRAC) property, an additional protection is the indemnification provided by §330 of Public Law 102-484, the National Defense Authorization Act for FY93. Under §330 indemnification, DoD indemnifies transferees and lessees of base closure property from legal action for releases or threatened releases of hazardous substances resulting from DoD activities. In addition to the protections DoD provides, the use of environmental insurance may provide added assurance about future liability and assist in attracting financing and stimulating investment in former DoD property.

§330 Indemnification of Transferees of Closing Defense Property

"In general...the Secretary of Defense shall hold harmless, defend, and indemnify in full persons and entities...from and against any suit, claim, demand or action, liability, judgment, cost or other fee arising out of any claim for personal injury or property damage (including death, illness, or loss of or damage to property or economic loss) that results from, or is in any manner predicated upon, the release or threatened release of any hazardous substance, pollutant or contaminant, or petroleum or petroleum derivative, as a result of Department of Defense activities at any military installation (or portion thereof) that is closed pursuant to a base closure law."

CASE STUDIES

Although environmental insurance and its use in conjunction with contaminated DoD properties is relatively new, it has been used to aid the redevelopment of several BRAC installations. A recent example is the Fleet Industrial Supply Center in Oakland (FISCO), California. FISCO exemplifies the use of environmental insurance where property has been transferred using Early Transfer Authority (ETA), with the LRA conducting the cleanup. Environmental insurance also facilitated redevelopment at Lowry Air Force Base in Colorado and the U.S. Army Research Laboratory in Massachusetts. These two properties provide examples of the use of environmental insurance in more traditional base closure transfers (i.e., cleanup completed by DoD before transfer). In either case, ETA or non-ETA, it is important for interested parties to understand the scope of environmental insurance products and their potential usefulness to the transactions under consideration.

FLEET INDUSTRIAL SUPPLY CENTER, OAKLAND, CALIFORNIA

The 530-acre FISCO was selected for closure in the 1995 BRAC round. The Navy transferred title of FISCO to the City of Oakland through the City's Board of Port Commissioners (the Port). The development will create new marine terminals and warehousing and cargo transfer facilities, allowing for increased business-related operations. A new shoreline park will provide greater public access to the waterfront. The Navy transferred FISCO to the Port using ETA, with the Port assuming responsibility for completing the environmental cleanup. After the Port has obtained regulatory concurrence on the cleanup, the Navy will issue the CERCLA section 120(h) covenant stating that all necessary remediation has been completed. The Navy agreed to pay the Port a fixed price to conduct the cleanup. Any amount over that price (except for catastrophic events and unexploded ordnance) is the financial responsibility of the Port.





The agreement between the Navy and the Port required the Port to either self-insure or purchase general liability insurance. The Port chose to purchase both cleanup cost cap and pollution legal liability insurance. The cost cap insurance will protect the Port from cost overruns and the legal liability coverage will insure the Port against unforeseen environmental conditions.

Point of Contact: Board of Port Commissioners, (510) 272-1100.

LOWRY AIR FORCE BASE, DENVER, COLORADO

Lowry, a former Air Force installation that was primarily used as a training center, was selected for closure in 1991 and subsequently closed in 1994. The 1,866-acre former base is located in the center of the Denver metropolitan area, about 15 minutes from downtown. Lowry is currently being transformed into a new community that includes residential housing, a golf course, commercial businesses, a town center, and educational resources. The Lowry Redevelopment Authority is redeveloping the property. Contaminants include petroleum, metals, and solvents in the groundwater and soil.

To protect itself during redevelopment and against future release of contamination, the Lowry Redevelopment Authority purchased a comprehensive environmental insurance policy with three main coverage components:

- Legal defense expense
- Pollution legal liability
- Remediation liability/cost cap.

Point of Contact: Lowry Information Center, (303) 313-1516.

U.S. ARMY RESEARCH LABORATORY, WATERTOWN, MASSACHUSETTS

The U.S. Army Research Laboratory, a 48-acre property, was established in 1816 as the Watertown Arsenal for the manufacture of cannons and artillery. The installation was selected for closure in 1988. From the 1960s to closure, Watertown was used primarily for research, development, and testing new materials for certain weapons systems. The installation closed on September 30, 1995. The site is intended to be used for research and development purposes, 645,000 square feet of office space.

Watertown's comprehensive environmental insurance policy provides three main coverage components:

- Remediation of pollution that occurs during redevelopment
- On-site and off-site bodily injury and property damage claims
- Related legal defense expenses.

Point of Contact: Local Redevelopment Authority, (617) 972-6417.

*We welcome and invite your comments on this fact sheet
as we seek to improve the information provided.
Please send comments to:*

**OADUSD (Environmental Cleanup)
3400 Defense Pentagon
Washington, DC 20301-3400**

*You can find this fact sheet and other information on DoD's
BRAC Environmental Cleanup Web Page:*

<http://www.dtic.mil/envirodod/brac/>